NO. 92-1860

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1993

DONALD WAYNE DOUGLAS AND
DOUGLAS DRILLING, INC., PETITIONERS

v.

FEDERAL DEPOSIT INSURANCE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION, NATIONSBANK OF TEXAS, N.A.

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QUESTION PRESENTED

Whether the right of a secured lender to pursue a non-judicial foreclosure under Texas law is a substantive right that, under the Rules Enabling Act, 28 U.S.C. 2072(b), cannot be abridged by the Federal Rules of Civil Procedure.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 5a-11a) is reported at 979 F.2d 1128. The opinion of the district court (Pet. App. 14a-17a) is unreported.[1]

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[1] The opinions reproduced in the appendix to the petition contain several omissions. As did the FDIC, this respondent has reproduced corrected versions of the relevant passages (with the portions omitted from the appendix to the petition italicized)

JURISDICTION

The judgment of the court of appeals was entered on December 30, 1992. A petition for rehearing was denied on February 3, 1993. Pet. App. 1a-2a. The petition for a writ of certiorari was filed on May 4, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

On October 2, 1987, Douglas Drilling, Inc. ("DDI") and Donald Wayne Douglas ("Douglas") each executed a promissory note in favor of First Republic Bank Abilene, N.A. ("FRBA"). The DDI note was secured by a security interest in oil and gas equipment and a deed of trust in an interest in oil and gas property. The Douglas note was secured by a deed of trust in an interest in oil and gas property and a security interest in stock of DDI. Douglas guaranteed the payment of the DDI note.

In early 1988, DDI and Douglas defaulted on the notes. Thereafter, on April 11, 1988, after the maturity of the notes, petitioners filed a class action against FRBA and others on the basis of prime rate fraud. The case was removed to federal court to be consolidated with two other similar actions against the same parties. FRBA filed an answer but did not assert any counterclaims on the notes.

On July 29, 1988, FRBA failed, and the Federal Deposit Insurance Corporation ("FDIC") was

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in the Addendum to this Brief. See Addendum, *infra*, 1a.

appointed as Receiver. On the same date, through a purchase and assumption transaction, FDIC, as Receiver, assigned certain FRBA assets (including the Douglas and DDI notes) to NCNB Texas National Bank, now known as NationsBank of Texas, N.A. ("NCNB"). Thereafter, an attempt was made by petitioners to join NCNB as a defendant in the class action. The attempt failed, and NCNB was never made a party to the class action.

FDIC, as Receiver, retained the liabilities of FRBA with respect to the claims of the petitioners in the class action, and remained a party to the class action, which was abated until 1990. In March 1990, on petitioners' motion for dismissal, petitioners' complaint in the class action was dismissed with prejudice. See Pet. App. 8a.

NCNB later made demand upon DDI to turn over the collateral to NCNB. In response to such demand, the petitioners filed this action in Texas state court on March 25, 1991, seeking declaratory judgment that they were not liable on the notes, and also asserted claims for intentional infliction of emotional distress and malice against NCNB for seeking enforcement of the security agreements. NCNB counterclaimed for recovery of the collateral.

In November 1991, NCNB assigned the two notes to the FDIC, in its corporate capacity, the current holder of the notes. On December 13, 1991, FDIC intervened in the action, and removed the case to federal district court. After removal, FDIC sought recovery of the amounts due on the notes and an order requiring DDI to turn over the collateral. See Pet. App. 2-3; Pet. App. 7a-8a, 16a.

On May 21, 1992, summary judgment was entered that the petitioners take nothing against NCNB and FDIC and that FDIC recover the amounts due on the notes and for specific performance of the security agreements. See Pet. App. 12a-13a. The district court rejected the petitioners' claims that NCNB and FDIC were barred from collecting on the notes because FRBA had failed to seek collection of the notes as a compulsory counterclaim in the class action. The district court noted that in Texas a borrower could not force the lender to waive its non-judicial foreclosure remedy by filing a lawsuit and arguing that the debt was uncollectible. See Pet. App. 15a.

The court of appeals affirmed this decision. See Pet. App. 5a-11a. The court held that Fed. R. Civ. P. 13(a), governing compulsory counterclaims, could not "abridge, enlarge or modify any substantive right," as such would violate the Rules Enabling Act. 28 U.S.C. 2072(b). See Pet. App. 9a. The court concluded that application of the compulsory counterclaim rule would abridge the lender's substantive right under Texas law to elect non-judicial foreclosure, and would enlarge the debtor's substantive rights by allowing them to force the lender to pursue judicial foreclosure. Accordingly, the court concluded that FRBA had not been required to assert counterclaims in the class action, and that the FDIC's actions on the notes were not barred. *Id.* at 11a.

ARGUMENT

The petitioners have not urged any error with respect to the denial of relief that they sought against NCNB in the trial court. The sole issue presented,

therefore, is whether Fed. R. Civ. P. 13(a) barred the FDIC's rights to collect on the notes.

In that regard, NCNB here adopts and incorporates, as if set forth herein, the brief for the Respondent in Opposition, the FDIC, and would join the FDIC in urging that the petition should be denied for the following reasons:

1. The federal rules of procedure are not to "abridge, enlarge or modify any substantive right." 28 U.S.C. 2072(b); see *Stewart Organization, Inc. v. Ricoh Corp.*, 487 U.S. 22, 27 n.5 (1988). The lower courts correctly determined that Texas law had granted to a noteholder a substantive right to control its remedies for collection of the debt, and that application of Rule 13(a) would deprive the noteholder of this substantive right.

To apply Rule 13(a) as requested by petitioners would not result in a regulation of procedure - i.e., "the judicial process for enforcing rights and duties recognized by substantive law and for justly administering remedy and redress for disregard or infraction of them." See *Sibbach v. Wilson & Co.*, 312 U.S. 1, 14 (1941). It would, in fact, destroy a private, bargained-for contractual right, and in its place allow the party who defaulted on the contract to control the means of redress for disregard of such contract.

2. No conflict exists with decisions of this Court or the court of appeals. Although numerous decisions are cited by petitioners, they are cited solely for their statements concerning public policy, the prevention of duplicitous lawsuits, and conclusiveness of judgments. No decision cited

considers whether Rule 13(a) would abridge a substantive right of a party, such as the selection of foreclosure remedies.

3. The Texas Supreme Court opinion of *Barr v. RTC*, 837 S.W.2d 627 (Tex. 1992) does not abrogate the *Kaspar* rule.[2] *Barr* merely adopted the transactional approach to *res judicata*, and held that dual attempts by a lender to collect the same note wou'd be barred. *Id.* at 631. The court did not consider, nor did it address, the *Kaspar* rule or whether its ruling would be permitted to modify substantive rights of lenders to elect between judicial and nonjudicial foreclosure.[3] No such ruling can be inferred in the court's opinion, nor is such argument sufficient to justify review by this Court. See *Bishop v. Wood*, 426 U.S. 341, 345-346 (1976).

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[2] The rule relied upon by the lower courts in this case is found in *Kaspar v. Keller*, 466 S.W.2d 326, 329 (Tex. Civ. App. - Waco 1971, writ ref'd n.r.e.). The *Kaspar* rule was adopted in *Stille v. Colborn*, 740 S.W.2d 42, 44 (Tex. App. - San Antonio 1987, writ denied); *Thurman v. FDIC*, 889 F.2d 1441, 1444-1445 (5th Cir. 1989); and *Phillips v. FDIC (In re Phillips)*, 124 B.R. 712, 717-718 (Bankr. W.D. Tex. 1991).

[3] Texas rules enabling statute, TEX. GOVERNMENT CODE ANN. § 22.004 (Vernon 1988), was not considered in *Barr*. It states that the rules cannot abridge, enlarge or modify the substantive rights of a litigant. *See also* Tex. R. Civ. P. 814 (relied upon by the court in *Kaspar*, 466 S.W.2d at 392).

In addition to the above, NCNB, as the owner and holder of the notes, was never a party to the proceeding which was dismissed with prejudice, even though an attempt was made by petitioners to join it. As a consequence, *res judicata* would not apply to NCNB or its assignee, FDIC. *See Martin v. Wilks*, 490 U.S. 755, 761 (1989) (no one will be bound by a judgment in which he is "not designated as a party or to which he has not been made a party by service of process").[4]

As a result of the lower courts' action being in all things proper, the attempts to collect on the notes were lawful, and no claims urged by the petitioners against NCNB could be maintained.

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[4] Nor does the privity rule apply in these circumstances. No prior judgment existed against FRBA at the time of the transfer of the notes to NCNB by the FDIC, as Receiver; NCNB did not "control" the class action or the FDIC, as Receiver, during the course of the class action; and NCNB's interests as the owner of the notes were not adequately represented by the FDIC, as Receiver, who only retained the liabilities arising out of the class action. See *Benson & Ford v. Wanda Petroleum Co.*, 833 F.2d 1172, 1174 (5th Cir. 1987) (describing the three circumstances where privity will apply); *Thurman*, 889 F.2d at 1446 (FSLIC, as receiver, was held not to be a virtual representative of FSLIC, in its corporate capacity); *Pernie Bailey v. FDIC*, 905 F.2d 79, 80 (5th Cir. 1990) (Receiver retains liabilities).

CONCLUSION

The petition for writ of certiorari should be denied.

Respectfully submitted,

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ADDENDUM

1. The second sentence of the second paragraph on Pet. App. 7a should read as follows:

> DDI and Douglas contend that FDIC/corp. cannot collect on the notes because FRBA, a prior holder of the notes, lost its right to collect on the *notes by failing to counterclaim to collect on the* overdue notes in prior litigation.

2. The second sentence of the paragraph carrying over the Pet. App. 8a to Pet. App. 9a should read as follows:

> Fed. R. Civ. P. 13(a) provides that a counterclaim is compulsory if it arises out of the transaction or occurrence that is the subject matter of the plaintiff's *claim. Under rule 13(a), FRBA'S debt* collection claims against DDI and Douglas might very well constitute compulsory counterclaims.

3. The penultimate sentence of the first full paragraph on Pet. App. 15a should read as follows:

> Neither have they controverted the *amounts due on the notes, the interest rate to be applied, or the* amount of attorneys' fees requested by FDIC.